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TO RUEHC/SECSTATE WASHDC 8496  
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INFO RUEATRS/DEPT OF TREASURY WASHDC  
RUEHNE/AMEMBASSY NEW DELHI 2201  
RUEHKA/AMEMBASSY DHAKA 1032  
RUEHIL/AMEMBASSY ISLAMABAD 8026  
RUEHKT/AMEMBASSY KATHMANDU 6200  
RUEHKP/AMCONSUL KARACHI 2383  
RUEHCG/AMCONSUL CHENNAI 8630  
RUEHBI/AMCONSUL MUMBAI 6065  
RUEHLMC/MILLENNIUM CHALLENGE CORPORATION

UNCLAS SECTION 01 OF 02 COLOMBO 000735

SENSITIVE

SIPDIS

STATE FOR SCA/INS, SCA/PB AND EEB/CBA  
COMMERCE FOR EROL YESIN  
CHENNAI FOR FCS

E.O 12958: N/A

TAGS: [ECON](#) [ETRD](#) [EAID](#) [CE](#) [PK](#)

SUBJECT: Pakistan-Sri Lanka FTA Presents Opportunities for U.S.  
Businesses

¶1. (U) Summary: Trade between Pakistan and Sri Lanka has increased significantly following signing of the Pakistan-Sri Lanka Free Trade Agreement in June 2005. Total trade in 2004 was valued at USD 147.4 million; by 2007 it grew to USD 233.4 million, an increase of 58 percent. As tariffs are reduced in coming years, trade is expected to continue to grow. U.S. companies currently operating or considering operations in Sri Lanka may take advantage of the FTA by adding value to goods in Sri Lanka and exporting -- duty free -- to the larger Pakistani market. End Summary.

#### Agreement Details

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¶2. (U) Following an initial framework agreement in 2002 and several rounds of bilateral negotiations, the Pakistan-Sri Lanka Free Trade Agreement (FTA) was finalized in February 2005 and implemented in June of the same year. At its inception, Pakistan offered duty free entry for 206 products from Sri Lanka. To date Pakistan has reduced tariffs by 67 percent on all other imports from Sri Lanka with the exception of garments, ceramic products, betel leaves, and natural cosmetics -- which have quotas or preferential rates -- and an additional 540 items included on a no-concession list. Sri Lanka initially offered duty free entry to 102 products from Pakistan. To date Sri Lanka has reduced tariffs by 40 percent on the balance of items and plans to completely phase out tariffs by 2010, excluding 697 items covered by its no-concession list. Sri Lankan quotas on basmati rice and potatoes will remain intact. Products must meet a minimum of 35 percent domestic value-added in order to be eligible for FTA trade benefits. (Note: For complete lists please go to: [http://www.doc.gov.lk/web/pakissrilanka\\_agreement\\_duty.php](http://www.doc.gov.lk/web/pakissrilanka_agreement_duty.php))

#### Scheduled Tariff Reductions Delayed Due to Budget Constraints

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¶3. (SBU) Both countries were scheduled to undergo the next phase of tariff reductions in June 2008. Sri Lanka was to reduce tariffs by 20 percent and Pakistan to completely eliminate them except for quota and no-concession items. However, to date neither government has implemented this phase of the FTA, in part due to delays by the GSL and, in part, due to a severe economic downturn in Pakistan and delays by the newly elected Government of Pakistan in announcing economic policy. According to GSL sources, the Finance Ministry delayed granting concessions primarily due to revenue concerns, as additional duty concessions would constrain the government's ability

to raise much-needed revenue. If and when Sri Lanka proceeds with reductions, Pakistan has promised to eliminate its remaining tariffs; however, given the current economic climate in Pakistan, the likelihood of this is uncertain, at least in the short-term.

14. (U) The FTA with Pakistan is not the only trade agreement to suffer this year. Pursuant to the March 2008 Indo-Sri Lanka FTA, Sri Lanka was to offer duty-free access for imports from India, with the exception of 1,180 no-concession items. However, these duties still remain in place.

Benefits to Date:  
Substantial Increase in Trade  
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15. (U) Pakistani exports to Sri Lanka grew by 65 percent and Sri Lankan exports to Pakistan by 40 percent from 2004 to 2007. During this same period, Sri Lanka's real GDP grew by 22 percent and Pakistan's by 30 percent. Pakistani cotton exported to Sri Lanka is at present the largest good traded, and it has experienced significant growth due to the FTA. In 2002, Pakistan exported USD 24.1 million in cotton to Sri Lanka; by 2006 cotton exports grew to USD 86.6 million - an increase of over 350 percent. Sri Lanka experienced strong growth particularly in export of natural rubber to Pakistan. In 2002 natural rubber exports were valued at USD 4.9 million; by 2006 they increased to USD 17.3 million. Other goods saw similar increases.

Potential Opportunities for U.S. Companies  
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15. (U) The Pakistan-Sri Lanka FTA provides good opportunities for U.S. exporters and foreign investors that are active, or interested in becoming active, in the region. U.S. businesses may be able to reduce their cost of doing business and increase profits by adding value to goods in Sri Lanka and then exporting -- duty free -- to the larger Pakistani market. Exports from Sri Lanka that have potential to be profitable include rubber products, ceramics, motorcycles, and motor parts.

Comment  
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17. (SBU) In addition to the Pakistan-Sri Lanka FTA and the Indo-Sri Lanka FTA, Sri Lanka is also party to the South Asia Free Trade Agreement (SAFTA) and Asia Pacific Free Trade Agreement (APTA). The country is ideally located at the crossroads between eastern and western trade routes and has an excellent port. Labor costs are relatively low and the work force is well-educated with a 91 percent literacy rate. Nevertheless, foreign direct investment (FDI) remains low as significant deterrents to investment remain; in 2007, Sri Lanka received only USD 734 million in FDI. The protracted ethnic conflict with the Liberation Tigers of Tamil Eelam (LTTE), combined with an inefficient governmental bureaucracy and concerns of corruption, spur investor uncertainty. If Sri Lanka is to utilize FTAs to maximum capacity, the GSL needs to promote a more investor-friendly climate, including a political, rather than military, solution to the LTTE conflict. Post encourages U.S. companies and investors interested in doing business in Sri Lanka to contact the Embassy and the American Chamber of Commerce in Sri Lanka ([www.amcham.lk](http://www.amcham.lk)) for further information.